Before the FEDERAL COMMUNICATIONS COMMISSION Washington, D.C. 20554 DOCKET FILE COPY ORIGINAL

In the Matter of)		DECEIVED
Implementation of the Non-Accounting)		RECEIVED
Safeguards of Sections 271 and 272 of the)	CC Docket No. 96-149	APR 1 4 1997
Communications Act of 1934, as amended)		
)		Federal Communications Commission
Implementation of the)		Office of Secretary
Telecommunications Act of 1996:)	CC Docket No. 96-150	
Accounting Safeguards Under the)		
Telecommunications Act of 1996)		

CONSOLIDATED REPLY TO THE OPPOSITIONS TO PETITIONS FOR RECONSIDERATION

Cox Communications, Inc. ("Cox"), by its attorneys, hereby submits its *Consolidated*Reply to the Oppositions to Petitions for Reconsideration that were filed on the Commission's

Orders in the above-captioned proceedings. In their oppositions the Bell Operating Companies

("BOCs") uniformly oppose Cox's request that the Commission adopt additional competitive safeguards for BOC entry into competitive businesses. Rather than acknowledge the

Commission's findings in other recent proceedings that current safeguards are inadequate to protect against anticompetitive BOC activity in many competitive markets, I the BOCs continue

^{1/} Cox has submitted a consolidated reply because of the interrelated nature of the competitive safeguards issues involved in the two above-captioned Orders. See Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, First Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-149, FCC 96-489 (released December 24, 1996) ("Non-Accounting Safeguards Order"); Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996, Report and Order, CC Docket No. 96-150, FCC 96-490 (released December 24, 1996) ("Accounting Safeguards Order"); (collectively the "Orders").

^{2/} See, e.g., Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services, Notice (continued...)

to claim that there simply are no competitive issues to be further examined. The Commission must not adopt the BOC view, especially because it ignores the fact that Congress plainly believed existing competitive safeguards were inadequate during the transition to local competition. The Commission should adopt further safeguards for BOC entry into competitive markets now, as part of its reconsiderations in these proceedings.

I. THE INCONSISTENCY IN COMMISSION STATEMENTS MUST BE RECONCILED IN FAVOR OF ADEQUATE SAFEGUARDS

Cox made a simple request in its *Petition*: that the Commission reconcile the *Orders* with the findings it has made in other dockets by adopting on reconsideration the competitive safeguards it has promised.^{3/} Alternatively, Cox requested that the Commission at a minimum state that its narrow findings in the *Orders* regarding the safeguards necessary for BOC entry into the competitive businesses specifically covered by the 1996 Act will not prejudice the work the Commission still has before it in pending rulemakings on commercial mobile radio services ("CMRS") safeguards and video cost allocation.^{4/}

^{2/ (...}continued) of Proposed Rulemaking, Order on Remand, and Waiver Order, WT Docket No. 96-162, FCC 96-319 (released August 13, 1996) ("CMRS Safeguards Notice") at ¶ 34; Allocation of Costs Associated with Local Exchange Carrier Provision of Video Programming Services, Notice of Proposed Rulemaking, CC Docket No. 96-112, FCC No. 96-214 (released May 10, 1996) ("Cost Allocation Notice") at ¶¶ 2-3.

^{3/} Cox Petition at 1-2.

^{4/} Id. at 2.

The BOCs characterize Cox's *Petition* as a request for increased regulation "as competition increases." This is an incorrect interpretation. As an initial matter, the local exchange market is not competitive, and thus any BOC pleas for minimal oversight of combined regulated and nonregulated activities in the local exchange market are highly premature.

Moreover, Congress specifically has provided in the 1996 Act for the implementation of competitive safeguards during the transition to competition. Finally, the Commission has repeatedly stated the need for additional safeguards to protect emerging local exchange competition.

Inexplicably, the Commission's findings in its CMRS and video cost allocation proceedings that safeguards are needed are inconsistent with its decisions here. Contrary to BOC claims, however, conflicting Commission "tentative conclusions" in these other dockets should not be ignored. Rather, the Commission must either reconcile the statements in favor of adequate safeguards, or explain why it has concluded in this proceeding that only those requirements reflected in the 1996 Act for specific competitive market segments are necessary, and no others.

Indeed, the BOC argument that the Commission need not address Cox's *Petition* here because the matters raised by Cox are before the Commission in other dockets merely shows the success the BOCs have enjoyed in stalling any progress on fashioning competitive safeguards that fit the new market paradigm. The video *Cost Allocation* proceeding, cited by BellSouth as

^{5/} See, e.g., BellSouth Opposition (Docket 96-150) at 8.

^{6/} See, e.g., SBC Opposition (Docket 96-149) at 13-14; BellSouth Opposition (Docket 96-150) at 8; SBC Opposition (Docket 96-150) at 5.

the proper forum for resolving current affiliate transaction and cost allocation rules, has been pending before the Commission for almost a year, while the issue of BOC video-telephony cost allocation rules has been before the Commission since at least 1993.^{2/} The CMRS safeguards docket also has been open since last summer, and Cox has been asking for adequate BOC-CMRS safeguards since the Commission first proposed PCS in its 1990 rulemaking.^{8/} Predictably, in all of these proceedings, the BOCs have strenuously argued that existing rules are either sufficient, or are far too restrictive.

Regulatory inaction only benefits the BOCs. U S West, for example, claims here that in accounting for the costs of its Omaha former video dialtone/now cable system it has "removed common costs in their entirety" from regulation, yet this assertion is flatly contradicted by U S West's August, 1996 Cost Allocation Manual amendment. In that amendment, U S West stated that it was retaining *all* common costs for its Omaha video dialtone "trial" on the regulated books

^{7/} See BellSouth Opposition (Docket 96-150) at 8. The Cost Allocation Notice was released on May 10, 1996. See also Application of US WEST COMMUNICATIONS, INC., For Authority under Section 214 of the Communications Act of 1934, as amended, to construct, operate, own and maintain facilities and equipment to provide video dialtone service in portions of the Omaha, Nebraska service area, Order and Authorization, 9 FCC Rcd 184 (1993) at ¶ 31 ("Our decision here does not finally establish the method for tracking and assigning costs to video dialtone.").

^{8/} The CMRS Safeguards Notice was released on August 13, 1996. Cox continued to raise these concerns, for example, in the context of Pacific Bell's PCS "safeguards" plan. See Pacific Bell, Nevada Bell, Pacific Bell Mobile Services and Pacific Telesis Mobile Services' Plan of Non-Structural Safeguards Against Cross-Subsidy and Discrimination, Comments of Cox Enterprises, Inc., GEN Docket No. 90-314 (filed August 16, 1995) at 22 ("Since its decision to allow LECs to provide PCS in their landline monopoly regions pursuant to non-structural safeguards, the Commission has followed a pattern of deferring decisions on critical competitive issues. . . . The Commission can no longer wait to engage in a major policy analysis on in-region LEC-PCS safeguards until a later time").

^{9/} US West Opposition (Docket 96-150) at 3.

pending resolution of the video *Cost Allocation* proceeding. US West excused its action at the time with the claim that these expenses, a figure approaching \$35 million, would not be used for telephony ratemaking. That is irrelevant. The fact remains that under *existing* safeguards, US West has not been required to allocate \$35 million worth of expenses to its new "cable" system.

II. THE RECORD SUPPORTS ADDITIONAL SAFEGUARDS

Those BOCs that do address the merits of Cox's arguments fall back on variations of the tired refrain that the current price cap regime, Part 64 rules, and the *Joint Cost Order* provide adequate competitive and consumer safeguards. Bell Atlantic/NYNEX, for example, states that the BOCs have demonstrated that a price cap regulated LEC "is no more able to cross-subsidize than an unregulated firm." This statement, however, does not prove that additional safeguards are unwarranted. Unregulated firms can and do cross subsidize to build market share, as when a company advertises an item below cost as a "loss leader" in hopes of generating additional sales. Unregulated firms cannot, however, maintain cross subsidies over time because the market will prevent them from recovering lost profits. The BOCs, by contrast, retain near-monopoly power over basic local exchange service. Consequently, absent sufficient safeguards, the BOCs can

^{10/} See In the Matter of US WEST, Inc. Revisions to Permanent Cost Allocation Manual, Reply Comments of US West, Inc., AAP 96-82 (filed September 16, 1996) at 2 ("[A]s joint network costs of providing video dialtone and other network services are under study in another... Commission docket, the CAM revisions did not deal with these costs at all.") (citation omitted).

^{11/} *Id*.

^{12/} Bell Atlantic/NYNEX Opposition (Docket 96-150) at 6-7 and Bell Atlantic/NYNEX Opposition (Docket 96-149) at 7.

still cross subsidize competitive with noncompetitive services, and market forces can do nothing to prevent such BOC behavior.

Cox has also demonstrated repeatedly that the current price cap regime does not, in fact, provide adequate protection against cross-subsidization. The Commission's most recent pronouncements reflect a greater awareness of this fact. The BOCs' continued insistence that price caps are the panacea for cross-subsidization ignores these important questions, and makes superficial any assurance they might want to provide that further regulatory action is not required.

Similarly, SBC and U S West continue to claim that the current Part 64 rules, adopted over 10 years ago in the *Joint Cost Order*, are sufficient to govern BOC expansion into businesses they were forbidden from entering when the rules were adopted. However, SBC and U S West ignore the fact that the genesis of Part 64 cost allocation was in an era where the only unregulated services were investments for adjunct services such as voice mail. The scope and scale of BOC investments in unregulated CMRS and video is unprecedented, as is the joint nature of these investments.

These changes raise serious questions about the continued efficacy of Part 64, but these questions, again, are simply ignored by the BOCs. U S West, for example, says only that "the

^{13/} See Cox Petition at 4-5.

^{14/} See, e.g., In the Matter of Access Charge Reform, Notice of Proposed Rulemaking, Third Report and Order, and Notice of Inquiry, CC Docket No. 96-262, CC Docket No. 94-1, FCC 96-488 (released December 24, 1996).

^{15/} SBC Opposition (Docket 96-150) at 4-7; US West Opposition (Docket 96-150) at 3-

Commission has already determined that the Part 64 rules are sufficiently flexible and expansive to cover nonregulated activities that have developed since adoption of the original rules." SBC states that "the cost allocation system is applicable to any nonregulated activities the BOC undertakes, where there are many or only a few. The number of activities or amount of investment has no material impact on the efficient functioning of an allocation mechanism." 17/

What the BOCs have not attempted, however, is to explain how rules adopted for a different era that lump together all BOC nonregulated activities into a single set of accounts are appropriate today. Whereas it may have been sufficient to group BOC nonregulated investments together when they were limited to specific activities not involving shared plant or facilities, the very diversity of current BOC nonregulated investments makes such treatment completely inadequate.

As Cox explained in its *Petition*, current rules allow, and provide incentives for, systematic cost misallocation between BOC regulated and non-regulated activities. The rules also fail to require BOCs to identify service-specific costs, giving reviewers no meaningful way to determine whether costs have been properly allocated or whether a carrier's forecast of relative use has been unreasonable. Further, because BOCs do not provide cost information that distinguishes between different non-regulated activities, detection of cross subsidization is

^{16/} US West Opposition (Docket 96-150) at 4.

^{17/} SBC Opposition (Docket 96-150) at 6.

^{18/} Cox Petition at 4-5.

virtually impossible. Cox has raised these issues before, and made specific proposals on how to address these problems in both the *CMRS Safeguards Notice* and the *Cost Allocation Notice*. Then, as now, the BOCs have not explained why these concerns are unwarranted. Rather, they continue to assert, as they have done here, that no further rules are required.

The Commission's unsupported statement that it "designed [the] cost allocation rules to accommodate the growth of . . . nonregulated activities" is likewise insufficient. The Commission must show that Part 64 is up to the task of detecting cross subsidization in an environment where BOCs are increasingly engaging in joint regulated and unregulated activities. The Commission must explain why a system that fails to provide competitors (and regulators) with a sufficient level of information to detect improper BOC cross subsidization is nevertheless sufficient to ensure that BOCs not "use services that are not competitive to subsidize services that are subject to competition."

III. BOC PLEAS TO WEAKEN THE RULES MUST BE REJECTED

Contrary to their claims that additional safeguards are unnecessary, the BOCs have shown every indication that they intend to allocate as many costs as possible to their regulated operations. For example, several of the BOCs support SBC's request that the Commission read existing rules narrowly not to require an exogenous adjustment when network investment costs

^{19/} Cox Petition at 6-8.

^{20/} Accounting Safeguards Order at ¶ 26.

^{21/ 47} U.S.C. § 254(k).

are reallocated from regulated to nonregulated accounts.^{22/} As AT&T points out, exogenous treatment is needed to reflect the fact that ratepayers should not have to bear the costs of network upgrades that were made for the purpose of anticipated BOC entry into new lines of business.^{23/} Additionally, as Cox pointed out in the video *Cost Allocation* proceeding, if plant that has been 100 percent regulated is now shared or even nonregulated, error has occurred in BOC forecasting (or the BOC has committed fraud).^{24/} Absent exogenous cost treatment, no correction mechanism would be in place to deter these types of BOC "mistakes."

The Commission recognized that exogenous adjustments to the price cap indices should "only be eliminated when competition in the local service market eliminates the need for cost allocation rules altogether." The Commission must stand firm on this point and reject SBC's request to cross subsidize its unregulated ventures. 26/

^{22/} See SBC Petition (Docket 96-150) at 10-14; Ameritech Opposition (Docket 96-150) at 6-7; BellSouth Opposition (Docket 96-150) at 6; Bell Atlantic/NYNEX Opposition (Docket 96-150) at 5.

^{23/} AT&T Opposition (Docket 96-150) at 3.

^{24/} Allocation of Costs Associated with Local Exchange Carrier Provision of Video Programming Services, Reply Comments of Cox Communications, Inc., CC Docket No. 96-112 (filed June 12, 1996) at 5-6.

^{25/} Accounting Safeguards Order at ¶ 265.

^{26/} The Commission should also adopt the clarification requested by Time Warner that Section 272 applies to BOC provision of video services. See Time Warner Petition (Docket 96-149). Despite BOC claims to the contrary, the provision of video programming is often interLATA, as with, for example, live-feed newscasts. Such programming may not be provided through an unseparated video programming affiliate without violation of Section 272.

V. CONCLUSION

The issue of adequate safeguards for BOC entry into competitive businesses is squarely before the Commission in these dockets. On reconsideration, the Commission has the authority, and the obligation as Congress has encouraged in the 1996 Act, to adopt sufficient safeguards. The Commission can do so now or it can do it in the other proceedings it has initiated. Cox urges the Commission to adopt effective competitive safeguards on reconsideration.

Alternatively, the Commission must, at a minimum, confirm that its determinations in these proceedings do not supersede the critical work the Commission must still complete to adopt adequate, competitive safeguards for CMRS and video competition.

Respectfully submitted,

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April 14, 1997

CERTIFICATE OF SERVICE

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